HECO RT-6
DOCKET NO. 03-0371

REBUTTAL TESTIMONY OF
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HAWAIIAN ELECTRIC COMPANY, INC.

Subject: Regulatory Policy Matters

INTRODUCTION

Q. Please state your name, position and business address.

A. My name is William A. Bonnet and I am the Vice President of Government and Community Affairs at Hawaiian Electric Company, Inc. ("HECO"). I am also a Vice President for Hawaii Electric Light Company, Inc. ("HELCO") and Maui Electric Company, Limited ("MECO"). My business address is 1001 Bishop Street, Suite 811, Honolulu, Hawaii.

Q. Have you previously submitted testimony in this proceeding?

A. Yes, I submitted written direct testimony and exhibits as HECO T-6.

Q. What will your rebuttal testimony cover?

A. My rebuttal testimony will:

1) Summarize the Companies' regulatory policy position regarding combined heat and power ("CHP") systems and the Companies' proposed CHP Program;

2) Summarize the Companies' position regarding the County of Maui's proposal regarding municipal wheeling and Hawaii Renewable Energy Alliance's ("HREA") comments regarding net energy metering;

3) Summarize the agreement reached among the Consumer Advocate, Kauai Island Utility Cooperative and HECO on the issues in this proceeding.

REGULATORY POLICY POSITION

Q. Please summarize the Companies' regulatory policy position regarding CHP systems and the Companies' proposed CHP Program.

A. The reasons for the Companies' proposed CHP Program are detailed in the CHP Program application filed in Docket No. 03-0366, and are summarized in Mr. Seu's testimony, HECO T-1 and HECO RT-1. I would like to emphasize

again why the proposed program is appropriate from a regulatory policy perspective.

Hawaii's electric utilities cannot just be in the business of offering central station generation, as they have been told by legislators, by regulators, by the press, by the public and by their customers. They must be able to offer their customers an expanded array of choices that promote the State's energy objectives of having a reliable and affordable energy infrastructure, while promoting energy efficiency and the use of renewable resources.

The objectives of promoting CHP should be to encourage energy efficiency, to accelerate the implementation of cost-effective CHP, to provide customer choices, and to take into account the interests of all customers. These are all utility objectives. Installing, owning, operating and maintaining CHP as a regulated utility will substantially further all of these objectives.

Q. How are the interests of all customers taken into account?

A. The interests of all customers are taken into consideration primarily by structuring the program of installing utility-owned CHP systems so that non-participating customers are not burdened. If the electric utility is allowed to participate in the CHP market as a regulated entity, the Commission must approve the Companies' Schedule CHP tariff filing, and/or individual CHP Rule 4 project filings, and the Commission, with input from the Consumer Advocate, has the authority to regulate the Companies to ensure that the interests of all customers are taken into consideration.

Q. Are there additional reasons that the Companies should be allowed to pursue their proposed CHP Programs and other CHP projects with customers under special service contracts (termed Rule 4 contracts) as soon as possible?

A. There are several reasons, one of which is primarily applicable to HECO. As discussed by Mr. Sakuda in HECO T-3 and HECO RT-3, HECO has an increasing need for firm generating capacity. Even with HECO's forecasted firm capacity contributions of the Companies' proposed CHP program, in combination with the energy efficiency and load management DSM program impacts, new firm capacity would be needed in 2006. Given the long lead-time required to install the next generating unit, it is not possible to have a unit installed and operating by 2006. Since the next generating unit cannot be installed by 2006, options to mitigate the effects of the higher peak forecasts, including being allowed to proceed with a CHP program and/or CHP installations as soon as possible, are necessary.

Q. Have there been recent events that support this increasing need on Oahu?

A. Yes. On October 12, 2004, HECO hit a new record high for electricity demand at 1,327 MW (gross), which came on the heels of a record peak the night before at 1,319 MW (gross), and represents a 3.3% increase in the peak demand over last year and 14 MW above the February 2004 peak forecast. On October 13, 2004, HECO asked Oahu customers to conserve electricity until after 9 p.m. to help avoid a power outage on the island. Oahu's reserves of power generation were very tight that day due to the hot weather and the reduced power generation available. Two HECO generators were not available due to unanticipated maintenance and a generating unit operated by an independent power producer that sells power to HECO was also unavailable. These events clearly illustrate HECO's increasing need for additional capacity.

Q. What are the other reasons for proceeding with the Companies' program applicable to all of the Companies?

A. As discussed in HECO T-6, the first reason is to be able to meet the reasonable needs and expectations of their customers. The second is to avoid negative impacts on non-participating customers due to the unnecessary loss of revenues if a customer installs a third-party CHP system.

With respect to the first point, there are a number of commercial customers that are ready to proceed now with CHP systems. Some of these customers want to install CHP in connection with expansions or renovations of their operations or facilities.

With respect to the second point, some customers may install third-party CHP systems rather than continue to wait for regulatory proceedings to conclude in "due course". As discussed in earlier testimonies, the Companies' proposed CHP Program is predicated not only on offering new energy-efficient options to commercial customers and addressing load growth, but also on protecting the interests of the Companies' non-participating customers. Simply stated, non-participating customers should be better off when the Companies own, operate and maintain cost-effective customer-sited CHP systems, than when the systems are installed by third-parties (and the electric revenue displaced by such systems are lost).

Q. Why should the Commission allow the Companies to at least proceed with specific Rule 4 contracts?

A. In opening this proceeding, the Commission indicated it may consider related matters on a case-by-case basis and recognized that it should not defer consideration of all related filings. Given the Companies' capacity needs, the needs of their customers, and the benefits offered by cost-effective CHP system installations, the Commission should consider the Rule 4 contracts the

Companies' plan to submit to the Commission, even if this proceeding has not been concluded.

Q. How would the Companies' proceed with CHP?

A. The Companies plan to file applications for approval of contracts entered into under Rule 4 of its Tariffs for the installation of CHP projects on a customer-by-customer basis. As discussed by Mr. Seu in HECO RT-1, HECO signed its first CHP agreement with Pacific Allied Products, a major plastics and Styrofoam manufacturer located in Campbell Industrial Park. The 20-year contract is to install, own operate, and maintain a CHP system on the Pacific Allied site consisting of two 250 kW diesel generators and a 100 ton absorption chiller. HELCO also signed a CHP agreement with Sheraton Keauhou Resort, a newly renovated hotel in Keauhou on the Big Island. The 20-year contract is to install, own, operate, and maintain a CHP system on the hotel site consisting of two 370 kwW diesel generators and a 95 ton absorption chiller. HECO and HELCO are preparing applications to submit to the Commission and the Consumer Advocate for review and approval of the contracts pursuant to Rule 4 of the Companies' tariff. The Companies strongly encourage the Commission to consider approving the Rule 4 contracts on a case-by-case basis, pending the outcome of this proceeding (and the CHP Program docket). The CHP systems installed pursuant to the contracts are an important part of addressing (1) the load growth situation, especially on Oahu, (2) the needs of our customers, and (3) the interests of non-participating customers.

Q. Do you have any other comments regarding the delay in implementing CHP by the Companies?

A. Delaying the start of the program for any significant period of time would

irrevocably harm ratepayers, the Companies and CHP Program customers. Load is growing faster than was anticipated, particularly on Oahu. Even with central station deferral benefits expected from their CHP programs, the need dates for new generation are sooner than new generation can be added to the system. The installation of utility-owned CHP systems can help avoid reserve margin shortfalls.

Issue No. 3

Q. Issue No. 3 addresses the roles of the regulated electric utility companies and the Commission in the deployment of distributed generation in Hawaii. What are the respective roles?

A. The roles of the utility and the Commission with respect to DG depend on the specific DG application. In response to Issue No. 1, Mr. Seu (HECO T-1) identified seven categories of DG application. The role of the utility with respect to each DG application is as follows:

1) Customer-sited emergency generation: A few mainland utilities have provided such service under tariff, with or without the right to use the emergency generators for peaking purposes when there is a capacity shortage, but the Companies do not currently anticipate providing such a service. Therefore, the role of the utility is to enforce tariff provisions, which require that such generation not be operated in parallel with the utility grid.

2) Substation-sited peaking generation: The Companies have used and intend to continue to use DG for this purpose under appropriate circumstances.

3) Substation-sited generation to address case-specific T&D problems: The Companies have implemented and intend to continue to implement DG for

this purpose in appropriate circumstances.

4) Customer-sited CHP systems: The Companies intend to offer CHP systems under circumstances where it is cost-effective for the utilities to do so, and offering such a service does not unduly burden non-participating customers. With respect to customer-sited CHP systems or other DG owned by the customers or third-parties, the utility's role is to develop and enforce interconnection standards, which the Companies have done by filing a Tariff Rule 14.H. The utility also provides back-up and supplemental service to the customers. The utilities must design and obtain approval for utility tariff provisions that ensure the utility customers will not be unduly burdened by the provision of utility back-up service to customers with customer-sited CHP systems or DG.

5) Customer-sited cogeneration: The Companies do not intend to offer such a service, but would consider owning such facilities on a case-by-case basis (for example, when such ownership would facilitate installation of a biomass plant that would contribute to meeting RPS goals). For non-utility cogeneration operated in parallel with the utility grid, the utilities develop and enforce interconnection standards, and provide back-up and supplemental service. Where excess power is exported to the utility system, the utilities negotiate power purchase and interconnection agreements based on Commission-adopted rules and principles enunciated by the Commission in power purchase dockets. As stated earlier, power purchase arrangements are beyond the scope of this proceeding.

6) Off-grid, customer-sited generation: The Companies do not intend to offer such a service. Thus, the utilities do not have a role in the deployment of

off-grid DG.

7) Customer-sited generation for power purposes only: The Companies do not intend to offer such systems, but would consider DG for this purpose on a case-by-case basis if such an application becomes a cost-effective utility option. The utility's role for non-utility DG is the same as its role for non-utility CHP systems.

Q. What would be the Commission's role with respect to each DG application?

A. With respect to utility proposals for substation-sited peaking generation and substation-sited generation to address case-specific T&D problems, the Commission's role is to review such proposals under paragraph 2.3.g.2 of General Order No. 7.

With respect to utility offerings of CHP systems, the Commission's role is to review the application for a CHP Program as it would other supply-side planning resources under the criteria included in the IRP Framework, and to review the proposed tariff provision (Schedule CHP, Exhibit E to CHP Program Application), the Eligibility Criteria (see, CHP Program Application, pages 31-33, and Exhibit E, Attachment I), and the program budget and budget flexibility provisions (CHP Program Application, pages 11-13) in order to determine whether the program will address its intended purposes. In the Companies' view, it is appropriate for contracts filed under an approved CHP Program to be reviewed under a file and suspend process, for the reasons explained in the CHP Program Application (pages 34-36).

The Companies also plan to request approval for the installation of CHP systems that may fall outside the scope of the CHP Program, and as stated earlier, for contracts entered into before the CHP program is approved. The

Commission's role would be to review applications for approval of the Rule 4 contracts under paragraph 2.3.g.2 of General Order No. 7 and to determine the consistency of these individual projects with the overall objectives of the CHP program (e.g., to review the consistency of the form of contract and the pricing structure with that included in the CHP Program).

In the case of CHP systems and DG operated in parallel with the utility's grid system, the Commission's role is to investigate the impacts of such DG on the utility system, as it is doing in this proceeding, and review utility tariff provisions relating to the interconnection of such facilities to the utility grid and the utility's provision of back-up and supplemental service, as the Commission has done in other proceedings.

Finally, in the case of customer-sited CHP systems and DG owned by third-parties, the Commission's role is to review whether the retail sale of electricity by such third-party owners falls within the purview of the public utility statutes. To date, the Companies have not take the position that these third-party owned installations should be regulated by the Commission, due to the relatively small number of such installations.

<u>County of Maui's County Wheeling Proposal</u>

Q. The County of Maui alleges that reasonable wheeling rates for the County of Maui would facilitate investments in renewable and energy efficient DG systems. (COM-T-1, page 13, lines 10-11.) What is HECO's response?

A. The County of Maui's proposal is beyond the scope of this proceeding. As stated in Order No. 20582, the purpose of the proceeding is to examine the potential benefits and impacts of distributed generation on Hawaii's electric distribution systems and market. Distributed generation involves the use of small scale

electric generating technologies installed at, or in close proximity to, the end-user's location. As stated in Order No. 20582, the objective of this proceeding is to develop policies and a framework for distributed generation projects deployed in Hawaii.

In addition, the County of Maui's county wheeling proposal raises issues associated with wholesale and retail competition. In Decision and Order No. 20584 issued in Docket No. 96-0493, the Commission's proceeding on electric competition, the Commission stated that "at best, implementation of retail access would be premature ... projections of any potential benefits of restructuring Hawaii's electric industry are too speculative and it has not been sufficiently demonstrated that all consumers in Hawaii would continue to receive adequate, safe, reliable, and efficient energy services at fair and reasonable prices under a restructured market at this time." Introduction of wheeling raises significant policy issues, which cannot be adequately addressed in the context of only MECO and the County of Maui, as suggested by the County of Maui. The implications of such a proposal would have to be clearly examined and understood, including the implications for the electrical system and equipment, impacts on all customers, and the impact on the reliability of the system.

Net Energy Metering

Q. HREA claims that the size limitations in Hawaii's net energy metering law was set without a detailed assessment of offsetting benefits that net metered systems provide. Does HECO have any comments to HREA's claim? (HREA-T-1, page 9. lines 1 to 7.)

A. The Companies' would simply note that the issue appears to be beyond the scope of this generic docket, which generally addresses the generic framework from a

utility regulatory perspective, for DG in Hawaii.

The net energy metering law was amended by Act 99, Session Laws of Hawaii, effective June 2, 2004. Under Act 99, the net energy metering law was amended to increase the size of the facilities qualifying for net energy metering from 10 kilowatts to 50 kilowatts. As HECO testified at the legislature, HECO supports the measured approach to increased penetration of net energy metering. This involves incremental increases in the allowed size of an installation followed by monitoring of participation and financial impact on non-participants. Toward that end, HECO supported expansion of the 10 kW limit to 50 kW this past legislative session, recognizing that the 50 kW amount may introduce interconnection considerations that are different than those associated with 10kW facilities. This was acknowledged in the final legislation. Any further changes at this time to the net energy metering limits would be premature, since the current legislative change has been in effect for less than a year. Any change would raise significant issues, which have not been addressed in HREA's testimony, and we consider to be beyond the scope of this docket..

Agreement among the Consumer Advocate and Kauai Island Utility Cooperative

Q. Has HECO discussed its position with the Consumer Advocate and Kauai Island Utility Cooperative ("KIUC")?

A. After the end of the settlement discussions with all parties on September 30, 2004, it was apparent that a settlement would not be reached with all parties at that time. However, the Consumer Advocate, in reviewing its position, determined that the Consumer Advocate and the utilities' positions were not very different, and that

there may be a possibility of an agreement. Discussions were held individually with HECO and KIUC. Attached as HECO-R-601 is a matrix of the issues and where the Consumer Advocate, KIUC and HECO's positions are noted. As shown on the attached matrix, HECO, KIUC and the Consumer Advocate's positions are aligned, or at least not in conflict, with respect to the issues in this proceeding.

SUMMARY

Q. Please summarize your testimony.

A. The Companies have provided seven testimonies to support the reasons for and benefits of utility participation in the provision of CHP systems. The provision of CHP services by utilities is a natural step in the evolution of electric utility services, and electric utility customers should have the option of acquiring CHP systems from Hawaii utilities. Mr. Seu, in HECO RT-1 reiterated why HECO should be allowed to participate in customer-sited DG projects as regulated utility. The Consumer Advocate supports HECO's participation and prefers that it be regulated (see HECO-R-601, page 3).

The Commission has already recognized that it should not defer consideration of all related filings to this proceeding. Given the load growth projections for Oahu, the needs of CHP customers, and the interests of all utility customers, the Commission should consider the Rule 4 contracts the Companies' plan to submit to the Commission.

Q. Does this conclude your testimony?

A. Yes, it does.